First National Stores Inc.

Finast

1975 Annual Report

FOR THE YEAR ENDED MARCH 29

Financial Highlights

	52 Weeks ended March 29, 1975	52 Weeks ended March 30, 1974
Sales	**$934,803,000**	$859,598,000
Income (loss) before extraordinary credits and before cumulative effect on prior years of change in accounting	**4,133,000**	(13,466,000)
Extraordinary credits	**1,575,000**	572,000
Cumulative effect of change in method of accounting	**—**	(1,964,000)
Net income (loss)	**5,708,000**	(14,858,000)
Per share of common stock:		
Income (loss) from operations	**3.32**	(9.81)
Extraordinary credits	**1.26**	.41
Cumulative effect of change in method of accounting	**—**	(1.43)
Net income (loss)	**4.58**	(10.83)
Capital expenditures	**9,781,000**	7,557,000
Net working capital	**18,375,000**	28,440,000
Total assets	**123,530,000**	134,568,000
Stockholders' equity	**63,874,000**	65,571,000
Book value per share	**56.49**	48.01
Number of stores (at year end)	**274**	320
Shares outstanding—weighted average	**1,246,315**	1,372,197
Shares outstanding (at year end)	**1,130,787**	1,365,774

Common Stock

Three dividends of twenty-five cents per share were declared in fiscal 1975 which were paid on September 12, 1974, December 6, 1974 and April 7, 1975.

The following table shows the high and low quarterly sales prices of the Company's common stock for fiscal years 1974 and 1975 on the New York Stock Exchange prior to February 18, 1974 and on the Boston Stock Exchange thereafter.

Fiscal Year		High	Low
1974	First quarter (April 1 through June 30)	18⅜	16¾
	Second quarter (July 1 through Sept. 29)	20	15¾
	Third quarter (Sept. 30 through Dec. 29)	21¾	15
	Fourth quarter (Dec. 30 through March 30)	27¾	18
1975	First quarter (March 31 through June 29)	26	23
	Second quarter (June 30 through Sept. 28)	26¾	20½
	Third quarter (Sept. 29 through Dec. 28)	27	20⅞
	Fourth quarter (Dec. 29 through March 29)	24½	20¾

Copies of the Company's Annual Report (Form 10-K) to be filed with the Securities and Exchange Commission may be obtained without charge upon request to Treasurer's Office, First National Stores Inc., 5 Middlesex Avenue, Somerville, Massachusetts 02143.

The Annual Meeting of Shareholders will be held at The Forum Room, State Street Bank Building, Fifth Floor, 225 Franklin Street, Boston, Massachusetts on Monday, June 23, 1975, 10:00 A.M. Eastern Daylight Time. All Shareholders are cordially invited to attend.

To Our Shareholders:

The results for fiscal 1975 show significant progress. Sales were $934,803,000 compared to $859,598,000 in fiscal 1974, an increase of 8.7%. Income before extraordinary credit was $4,133,000 or $3.32 per share. In fiscal 1974, loss before extraordinary credit and after the effect of a change in method of accounting for costs related to store closings was $13,466,000 or $9.81 per share.

Net income for fiscal 1975 was $5,708,000 or $4.58 per share after giving effect to an extraordinary credit of $1,575,000 or $1.26 per share resulting from the utilization of available net operating loss carryforwards. Net loss in 1974 was $14,858,000 or $10.83 per share after giving effect to an extraordinary gain of $572,000 on the sale of land and a charge of $1,964,000 for the cumulative effect on prior years of the change in method of accounting for costs related to store closings.

At the end of fiscal 1975 the company, a food supermarket chain, had 274 stores in operation throughout New England and in the metropolitan area of New York including northern New Jersey. This represents a reduction of 46 stores or 446,260 square feet of selling area from the close of fiscal 1974 and substantially completes the accelerated closing of older and outmoded stores announced in that year.

During fiscal 1975 fourteen stores received major remodels and ten others were modernized. Remodels in many instances consisted of expansion of sales areas and in all instances included installation of new and more efficient fixtures and modern decor. In the current year five new stores are either under construction or under agreement to be constructed. We also continue to place great priority on remodeling existing units with ten major and eleven other remodels already underway. Many more are on the drawing boards.

The company is in a strong financial position to carry out its store improvement program as an examination of our balance sheet shows. At the end of fiscal 1975, cash and short term investments were $27,400,000 and a $4,000,000 receivable is to be paid prior to June 30, 1975. In fiscal 1975 the company paid off all its loans totaling $10,058,000 and is free of debt at this time. Also, on September 29, 1974, the company acquired through a tender offer 235,966 shares of its common stock at a cost of approximately $6,500,000 including expenses of the tender. There remained 1,130,787 shares of common stock outstanding at year end. Three dividends of 25¢ each were declared during the year.

In fiscal 1975 management concentrated its efforts on reducing overhead costs and on the refinement of the company's total operations. As a part of our strategy to decentralize profit responsibility the former New York and Somerville Divisions were divided into four separate divisions. This has resulted in closer control of our store operations by field management and a greatly enhanced ability to respond quickly to local merchandising requirements. The consolidation of our warehousing and transportation functions into two distribution centers, one in Somerville, Massachusetts and the other in South Kearny, New Jersey, was completed and expected economies are being realized. A major investment was made in the modernization of our transportation fleet completing a renewal program begun two years earlier which has increased delivery efficiency and reduced fleet operational costs. The extensive renovation and enlargement of our East Hartford bakery is almost complete and the company's total bakery production facilities are now centralized at this location.

Every overhead responsibility center has been reviewed in depth. Personnel reductions have been accomplished and improved organizational methods adopted. We have strengthened our corporate and divisional groups by employment of experienced, high caliber staff.

We have continued to refine individual store budgeting and planning by store managers and field personnel. This is the key to our success in building our business on a store by store basis with each store being responsible for its own performance.

The program outlined above has made us more effective in responding quickly to the needs of our business.

Further significant steps taken during the year included: the accomplishment of a planned reduction in warehouse and store inventory of approximately $10,000,000 at current costs; enlargement of our Market Research Department; institution of an additional training program in store management; and the reorganization of the Personnel Department to improve recruiting, manpower planning and the effectiveness of the company's equal employment opportunity program.

Electronic ordering systems have been installed in most of our stores and it is expected that installation will be completed in all stores by mid-summer. These systems facilitate and increase the speed of merchandise ordering and will also be used for transmitting other data such as payroll and accounting information by year end. We began installation of electronic cash registers. These are faster and generate greater information than their electro-mechanical counterparts. They are also compatable with the utilization of computers and scanners at store level. We are presently testing a full-scale automated check-out system which so far gives great promise for the future.

We have expanded our advertising on radio and television and have brought a new look to our newspaper ads. Innovative sales promotion efforts such as "The Finast Way" and "Meat Street—USA" have been our major new themes. Supporting these promotional efforts are several consumer programs including the following: we were the first in our market area to eliminate raising prices of merchandise already on our shelves; we instituted new and exacting trim standards in conjunction with a double-your-money-back quality guarantee on meat; we developed a new unit price label that contains the old as well as the new price to allow customers to follow price changes; we placed the last date of sale on the labels of all perishable products and continue to expand open coding on grocery items.

The net result of the year was to position the company so that it can meet the requirements of the marketplace promptly and efficiently. This is especially important today when the customer, due to money pressures and inflation, is more selective and more responsive to price changes. With limited dollars to spend, customers look for real value and we find them trading down and innovating as they attempt to feed their families within their budgets without sacrificing nutritional value. We are especially pleased with the ability of our merchandisers to adapt to this new environment.

It is difficult to speculate on next year's results. Our industry is faced with vastly increased and intricate federal, state and local legislation. The differences in such legislation from jurisdiction to jurisdiction are causing us to experience increased operational, administrative and legal costs. Energy costs, which rose 50% last year, are expected to continue their extraordinary rise. Labor costs continue to increase and challenge our ability to compensate with improved productivity. Of immediate concern is a strike we are currently experiencing at our Somerville distribution base. All of our company stores are open despite the strike but we are unable at this time to state what its effect will be on fiscal 1976 results. Despite these concerns, we are pleased with last year's performance and feel ourselves stronger than any time in the last ten years as we face this year's challenges.

Respectfully submitted,

William T. French | Alan L. Haberman

William T. French
Chairman of the Board

Alan L. Haberman
President and Chief Executive Officer

FIRST NATIONAL STORES INC.

Consolidated Statements of Income (Loss) and Retained Earnings

	52 Weeks ended March 29, 1975	52 Weeks ended March 30, 1974
Sales	**$934,803,000**	$859,598,000
Costs and expenses:		
Cost of sales (Note 4), warehousing, transportation and store occupancy expenses	**790,220,000**	735,148,000
Direct selling, advertising, general and administrative expenses	**134,121,000**	123,707,000
Depreciation and amortization (Note 2)	**6,731,000**	6,622,000
Estimated charges (credits) related to store closings (Notes 2 and 5)	**(449,000)**	8,560,000
	930,623,000	874,037,000
Operating income (loss)	**4,180,000**	(14,439,000)
Other income (expense):		
Interest income	**2,487,000**	2,107,000
Interest expense including imputed interest of $481,000 in 1975 and $251,000 in 1974	**(933,000)**	(1,242,000)
Other	**199,000**	108,000
	1,753,000	973,000
Income (loss) before federal and state income taxes	**5,933,000**	(13,466,000)
Federal and state income taxes (Note 9)	**1,800,000**	–
Income (loss) before extraordinary credits and before cumulative effect on prior years of change in accounting	**4,133,000**	(13,466,000)
Extraordinary credits:		
Utilization of net operating loss carryforward (Note 9)	**1,575,000**	–
Gain on sale of land	**–**	572,000
Cumulative effect on prior years (to March 31, 1973) of change in method of accounting for costs related to store closings, less $1,158,000 tax effect (Note 5)	**–**	(1,964,000)
Net income (loss)	**5,708,000**	(14,858,000)
Retained earnings at beginning of year	**44,576,000**	59,434,000
Cash dividends declared – $.75 per share in 1975	**(907,000)**	–
Retained earnings at end of year	**$ 49,377,000**	$ 44,576,000

Per share of common stock (Note 2):		
Income (loss) before extraordinary credits and cumulative effect of change in accounting	**$3.32**	$ (9.81)
Extraordinary credits	**1.26**	.41
Cumulative effect of change in method of accounting for store closings (Note 5)	**–**	(1.43)
Net income (loss)	**$4.58**	$(10.83)

Pro forma amounts assuming the change in method of accounting for costs related to store closings had been applied retroactively (Note 5):		
Income (loss) before extraordinary credits		$(13,466,000)
Per share of common stock		(9.81)
Net income (loss)		(12,894,000)
Per share of common stock		(9.40)

FIRST NATIONAL STORES INC.

Consolidated Balance Sheets

	March 29, 1975	March 30, 1974
Assets		
Current assets:		
Cash	**$ 5,431,000**	$ 5,309,000
Short-term investments, at cost which approximates market	**22,003,000**	25,942,000
Accounts receivable, less allowance for doubtful accounts—$300,000 in 1975 and 1974	**5,776,000**	5,329,000
Amounts due on sale of equipment (Note 3)	**4,102,000**	—
Inventories (Notes 2 and 4)	**32,822,000**	46,095,000
Prepaid expenses and other current assets	**2,971,000**	2,843,000
Total current assets	**73,105,000**	85,518,000
Fixed assets, at cost (Note 2):		
Land	**3,367,000**	3,572,000
Buildings owned	**11,938,000**	16,237,000
Store fixtures and equipment	**69,279,000**	65,300,000
Leasehold improvements	**13,687,000**	12,013,000
Other machinery and equipment	**20,001,000**	19,141,000
	118,272,000	116,263,000
Less—Accumulated depreciation and amortization (Note 2)	**70,257,000**	68,728,000
	48,015,000	47,535,000
Other assets and deferred charges	**2,410,000**	1,515,000
	$123,530,000	$134,568,000
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	**$ 38,583,000**	$ 35,768,000
Dividends payable	**283,000**	—
Accrued expenses	**14,404,000**	16,609,000
Current portion of long-term debt	**—**	3,267,000
Current portion of accrued costs related to store closings (Notes 2 and 5)	**1,460,000**	1,434,000
Total current liabilities	**54,730,000**	57,078,000
Long-term debt (Note 6)	**—**	6,791,000
Accrued costs related to store closings (Notes 2 and 5)	**3,525,000**	4,334,000
Other deferred credits	**1,401,000**	794,000
Stockholders' equity (Notes 1, 7 and 8):		
Common stock, without par value:		
Authorized—5,000,000 shares		
Issued—1,655,268 shares	**31,874,000**	31,872,000
Retained earnings	**49,377,000**	44,576,000
	81,251,000	76,448,000
Less—Treasury stock, at cost—524,481 shares in 1975 and 289,494 shares in 1974 (Note 12)	**17,377,000**	10,877,000
	63,874,000	65,571,000
Lease commitments (Note 10)		
	$123,530,000	$134,568,000

FIRST NATIONAL STORES INC.

Consolidated Statements of Changes in Financial Position

	52 Weeks ended March 29, 1975	52 Weeks ended March 30, 1974
Financial resources were provided by:		
Operations:		
Income (loss) before extraordinary credits and cumulative effect of change in accounting	**$ 4,133,000**	$(13,466,000)
Expenses not requiring outlay of working capital in the current period:		
Depreciation and amortization (Note 2)	**6,731,000**	6,622,000
Estimated charges (credits) related to store closings	**(266,000)**	7,062,000
Other, including deferred compensation accrual in 1975	**634,000**	(18,000)
Working capital provided by operations	**11,232,000**	200,000
Extraordinary credits:		
Utilization of net operating loss carryforward	**1,575,000**	—
Proceeds from sale of land	**—**	3,214,000
Cumulative effect of change in accounting, less amounts not affecting working capital	**—**	(2,420,000)
Proceeds from disposal of fixed assets	**2,192,000**	4,253,000
	14,999,000	5,247,000
Financial resources were used for:		
Additions to fixed assets	**9,781,000**	7,557,000
Acquisition of treasury stock	**6,533,000**	—
Reduction in long-term portion of accrued costs related to store closings	**1,092,000**	—
Reductions of long-term debt (including in 1974, $1,947,000 related to mortgage notes assumed by buyer, secured by land sold) (Note 6)	**6,791,000**	5,395,000
Cash dividends declared	**907,000**	—
Change in other noncurrent assets	**(74,000)**	179,000
Other	**34,000**	121,000
	25,064,000	13,252,000
Increase (decrease) in working capital	**(10,065,000)**	(8,005,000)
Working capital at beginning of year	**28,440,000**	36,445,000
Working capital at end of year	**$ 18,375,000**	$ 28,440,000
Analysis of changes in elements of working capital:		
Increase (decrease) in current assets:		
Cash and short-term investments	**$ (3,817,000)**	$ 2,334,000
Accounts receivable	**447,000**	(3,822,000)
Amount due on sale of equipment	**4,102,000**	—
Inventories (Notes 2 and 4)	**(13,273,000)**	(282,000)
Prepaid expenses and other current assets	**128,000**	(542,000)
	(12,413,000)	(2,312,000)
(Increase) decrease in current liabilities:		
Accounts payable	**(3,098,000)**	146,000
Accrued expenses	**2,205,000**	(2,188,000)
Current portion of long-term debt	**3,267,000**	(2,217,000)
Current portion of accrued costs related to store closings (Note 5)	**(26,000)**	(1,434,000)
	2,348,000	(5,693,000)
Increase (decrease) in working capital	**$(10,065,000)**	$ (8,005,000)

Notes to Financial Statements

Note 1 – Principal Stockholder

During February 1974, Madison Fund, Inc. acquired, through a tender offer, 346,103 shares of the Company's common stock which, together with 350,900 shares previously held, resulted in Madison Fund owning 51% of the Company's outstanding shares at March 30, 1974.

As described in Note 12, during September 1974, the Company, through a tender offer, reacquired 235,966 shares of its common stock, resulting in a comparable reduction of outstanding shares and an increase in Madison Fund's ownership to 61.6%.

Note 2 – Summary of Significant Accounting Policies

The accounting and reporting policies of First National Stores Inc. conform with generally accepted accounting principles. The following describes the more significant of those policies:

Consolidation Policy

All subsidiaries of the Company are included in the consolidated financial statements. Significant intercompany transactions and balances are eliminated.

Inventories

Inventories are stated at cost or market, whichever is lower, cost being determined substantially by the last-in, first-out method of inventory valuation (see Note 4).

Depreciation and Amortization

For financial statement purposes, depreciation and amortization are computed by the straight-line method except for assets acquired during the period March 1954 to March 1966. For assets acquired during this period, depreciation is computed primarily by the sum-of-the-years digits method. For tax purposes, accelerated depreciation methods are generally used. Estimated useful lives are as follows:

Buildings owned	20-50 years
Store fixtures and equipment	3-10 years
Leasehold improvements	15-25 years
Other machinery and equipment	3- 8 years

Maintenance and Repairs

Expenditures for maintenance, repairs and minor renewals are expensed in the year in which incurred, while betterments and major renewals are capitalized.

Store Closing Costs

Beginning in fiscal 1974, estimated future expenditures related to store closings, principally rents, real estate taxes and other occupancy costs, net of estimated income from existing sublease arrangements, together with the unamortized value of leasehold improvements and store equipment, are charged to income when the decision is made to close the store. Gains on dispositions of store properties are recognized when realized. Prior to 1974, store fixed assets were expensed when the store was closed while occupancy costs were expensed when they became payable (see Note 5).

Pre-Opening Expenses

All expenses incurred in connection with the opening of stores are charged to income as incurred.

Income Taxes

The provision for income taxes in the financial statements relates to the items of income and expense included in such statements. Deferred income taxes are provided when necessary to recognize the effects of timing differences which result when items of income or expense are recognized in a different period for tax purposes. The investment tax credit arising from the purchase and lease of qualifying property additions is recognized under the "flow through" method (see Note 9).

Net Income (Loss) Per Share

The weighted average number of shares used to compute net income (loss) per share includes the shares allotted but not yet issued under the Company's previous executive incentive compensation plan (see Note 8) and, if the effect is dilutive, the shares issuable under the stock option plan (see Note 7).

Pensions

The Company maintains a trusteed non-contributory pension plan for employees who are not covered by union pension plans. Actuarial gains, resulting principally from the transfer of employees to various union plans and appreciation in the fund, are being amortized over ten-year periods from the dates of occurrence (see Note 11).

Note 3 – Amounts Due on Sale of Equipment

Amounts due on sale of equipment at March 29, 1975 represent the proceeds due on the sale, at net book value, of certain new manufacturing equipment.

In accordance with the terms of an agreement dated May 2, 1975, the Company has agreed to lease back the equipment over terms ranging from three to ten years.

Note 4 – Inventories

Inventories stated under the LIFO method were $28,070,000 and $24,754,000 less than current average costs at March 29, 1975 and March 30, 1974, respectively.

During 1975, there was a reduction in inventory levels which caused a liquidation of LIFO inventory quantities carried at the lower costs prevailing in prior years and as a result, cost of sales in fiscal 1975 has been reduced by $4,277,000.

Note 5 – Costs Related to Store Closings

The change in accounting for costs related to store closings was reflected as of the beginning of fiscal 1974 and the effect on that year was to increase the loss before extraordinary items by $6,383,000 ($4.65 per share). The 1974 net loss also includes an adjustment of $3,122,000 to apply retroactively the new method (the "cumulative effect"), which amount has been reduced by the reversals of deferred income taxes provided in prior years. The pro forma amounts shown on the income statement for 1974 have been adjusted for the effects of retroactive application had the new method been employed during fiscal 1973.

At March 29, 1975 and March 30, 1974 accrued costs related to store closings were as follows (000 omitted):

	March 29, 1975		March 30, 1974	
	Current Liability	Long-term Liability	Current Liability	Long-term Liability
Estimated future costs related to store closings	$1,945	$4,538	$2,099	$6,034
Less-imputed interest at weighted average rate of 12% in 1975 and 11% in 1974	485	1,013	665	1,700
Accrued costs	$1,460	$3,525	$1,434	$4,334

At March 29, 1975 estimated payments of these costs, less imputed interest, during each of the next five fiscal years are as follows: 1976 $1,460,000; 1977 $927,000; 1978 $596,000; 1979 $449,000; and 1980 $293,000.

Estimated credits related to store closings, as shown on the statement of income for 1975, are principally the result of recognizing gains on the disposal of closed store properties and equipment in the period such gains are realized together with the net effect of revised estimates regarding store closings.

Note 6 – Debt Repayment

At March 30, 1974, long-term debt, which was prepaid during 1975, consisted of the following (000 omitted):

4.70% Notes	$ 1,058
Bank loan	9,000
	10,058
Less – current portion	3,267
Total long-term debt	$ 6,791

Interest on the bank loan was paid at a weighted average rate of 11.6% during fiscal 1975.

Notes to Financial Statements (continued)

Note 7—Stock Options

Under the Company's stock option plans, options may be granted to key employees to purchase common stock at not less than the fair market value on the date of grant. Of the options outstanding on March 29, 1975 options for 2,000 shares were then exercisable; 30,500 shares were available for future options.

The following table summarizes the stock option activity during 1975:

	Number of shares	Price per share
Options outstanding at beginning of year	35,800	$17.50 to $30.25
Granted	6,500	$24.875 to $25.25
Expired or terminated	(9,800)	$17.50 to $30.25
Options outstanding at end of year	32,500	$17.50 to $30.00

Note 8—Incentive Compensation Plans

The stockholders approved in 1970 an executive incentive compensation plan under which 6% of pre-tax income, as defined, was available for awards to eligible participants in any year through fiscal 1975 in which such income exceeded $3,000,000 and cash dividends on common stock were paid. In accordance with the provisions of that plan, no compensation was recorded for fiscal years 1972 through 1974. Under previous awards, 979 shares of treasury stock were issued during 1975 and 821 shares in 1974. The difference between the amount of compensation accrued and the average cost of treasury shares so issued was (credited) charged to the common stock account in the amounts of ($2,000) and $2,000 in 1975 and 1974, respectively. At March 29, 1975, a total of 5,603 shares allotted but not issued are issuable in future years.

During 1975, the Board of Directors terminated the earlier plan and adopted, subject to approval of the stockholders, a new executive incentive compensation plan. Under the new plan, 6% of pre-tax income, as defined, will be available for cash awards to eligible participants. Such amount cannot exceed the aggregate of the base compensation of the participants nor an amount which would reduce defined pre-tax income below $4,000,000; $590,000 has been provided during 1975 under the new plan in anticipation of stockholder approval.

Effective October 10, 1974, the Board of Directors adopted, subject to stockholder approval, a Performance Improvement Plan and authorized an aggregate of 100,000 "performance units" which may be granted to key executives. At March 29, 1975, 76,500 units had been granted. The plan provides for incentive compensation essentially equivalent to the amount by which the market value, as defined, of the performance units at the distribution date exceeds $27, the initial base value. Compensation under the plan is payable three years from the date of grant. At March 29, 1975, no compensation was accruable under this plan. This plan supersedes the incentive compensation provisions of the employment contract with the Chairman of the Board.

Note 9—Income Taxes

At March 29, 1975, the Company had approximately $10,400,000 of tax basis net operating loss carryforwards which expire principally in 1979. For financial accounting purposes, the operating loss carryforwards are approximately $11,800,000. The excess of the accounting basis carryforwards results principally from estimated costs related to store closings which are not currently deductible less the effect of accelerated depreciation used for tax purposes and other differences between tax and accounting income; the tax effect of these differences will be applied to deferred tax accounts to the extent they are realized.

In addition, the Company had a tax basis investment credit carryover of approximately $2,700,000 expiring at various dates through 1982. For financial accounting purposes the investment credit carryover is

$1,400,000; the difference results from the utilization of $600,000 of 1975 credits and $700,000 of credits relating to prior year property additions in calculating the 1975 provision for income taxes.

A reconciliation of the statutory federal income tax rate on income before income taxes to the effective rate follows:

Statutory rate	48 %
Less—effect of investment tax credits	(22)
Add—provision for state income taxes	4
Effective rate	30 %

Note 10—Lease Commitments

At March 29, 1975, the Company was committed under long-term leases for operating stores and other real property used in the business. These leases expire principally within ten to fifteen years and generally contain renewal options. The Company also leases motor vehicles and equipment. Costs related to closed stores, including an amount for future rent costs to the estimated disposal dates, are accrued in the financial statements.

The Company has determined that substantially all real estate leases and certain equipment leases are non-capitalized "financing leases" as defined by the Securities and Exchange Commission.

A summary of rent expense, excluding rents charged to accrued costs related to store closings, follows (000 omitted):

	1975	1974
Non-capitalized financing leases:		
Minimum rent	$10,733	$11,322
Additional rent based on sales	594	435
	$11,327	$11,757
All leases:		
Minimum rent	$12,939	$13,149
Additional rent based on sales	594	435
	$13,533	$13,584

Minimum annual rentals at March 29, 1975 under noncancelable leases for open store properties and leased equipment are as follows for the years or periods indicated (000 omitted):

Fiscal year	All leases	Financing leases
1976	$10,925	$ 9,764
1977	9,948	9,161
1978	9,277	8,546
1979	8,107	7,387
1980	7,073	6,412
1981-1985	26,336	24,829
1986-1990	17,820	17,820
1991-1995	9,464	9,464
After 1995	2,178	2,178

The present value of minimum lease commitments for noncapitalized financing leases are presented in the following table. Commitments for gross leases have been reduced by estimated real estate taxes and other operating expenses included in the gross payments.

	1975	1974
	(000 omitted)	
Operating store properties	$47,000	$52,300
Transportation equipment	1,400	2,000
	$48,400	$54,300

The weighted average interest rates used in these present value calculations were 7.4% for 1975 and 7.5% for 1974. The ranges of rates used were from 3.75% to 10% in both 1975 and 1974 for store properties. For transportation equipment the ranges were 5.25% to 12.25% in both years.

If, instead of recording rent expense, all financing leases were capitalized, related assets were amortized on a straight-line basis and interest costs were accrued on the basis of the outstanding lease liability, the impact on income before extraordinary credits would be to increase such amount by $322,000 in 1975. The impact in 1974 was insignificant. Included in this computation for 1975 was amortization of $4,600,000 and interest cost of $3,700,000; for 1974, the comparable amounts were $4,600,000 and $4,000,000, respectively.

Notes to Financial Statements (continued)

Note 11 – Pensions

The assets of the Company's pension fund exceed the actuarially computed value of plan liabilities. Since 1966, no charges have been required for pension costs, other than contributions to union pension plans, because recognized actuarial gains have exceeded the annual provisions for normal or current costs. Total pension costs charged to earnings, representing contributions to union plans, were $3,328,000 in 1975 and $2,977,000 in 1974.

The effects of the Employee Retirement Income Security Act of 1974 on future pension costs are not presently determinable.

Note 12 – Tender Offer

On September 12, 1974 the Company offered to purchase up to 200,000 shares of its common stock for $27 per share plus such additional number of shares properly tendered as the Company, in its discretion, should choose to purchase. The Company purchased 235,966 shares, representing all shares tendered, for approximately $6,371,000 plus expenses of approximately $162,000, which amounts have been charged to treasury stock.

Report of Independent Accountants

To the Board of Directors and Stockholders of First National Stores Inc.

We have examined the consolidated balance sheets of First National Stores Inc. and its subsidiaries as of March 29, 1975 and March 30, 1974 and the related consolidated statements of income (loss) and retained earnings and of changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

As described in Note 5 to the financial statements, in 1974 the Company changed its method of accounting for costs related to store closings.

In our opinion, the consolidated financial statements examined by us present fairly the financial position of First National Stores Inc. and its subsidiaries at March 29, 1975 and March 30, 1974 and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied during the period subsequent to the change, with which we concur, made as of April 1, 1973, referred to in the preceding paragraph.

PRICE WATERHOUSE & CO.

225 Franklin Street
Boston, Massachusetts 02110
May 12, 1975

Management's Discussion and Analysis of the Summary of Operations

Fiscal 1975 Compared to Fiscal 1974

In fiscal 1975 sales of $934,803,000 were $75,205,000 or 8.7% above those of fiscal 1974. The net increase in sales was a function of three factors: 1.) the impact on selling prices of inflation, 2.) the effect of heavier promotion and better customer acceptance in identical stores; i.e., stores that were open for the full period 1974 and 1975, and 3.) the closing of 46 stores during the year.

Cost of sales were down by 1% in relation to sales between fiscal 1975 and fiscal 1974. Gross margins in 1975 were favorably impacted by the government's decontrol of prices in April, 1974. Controls had caused sales mix abnormalities resulting in reduced gross margins in 1974. Also, a reduction in inventory levels resulted in a credit to cost of goods sold of $4,277,000 in 1975 as described in Note 4 to the Financial Statements. Warehouse and transportation costs were lower in 1975 with overall cost control more than compensating for greatly increased fuel and supply expenses. Store occupancy costs improved due to increased volume per unit and the reduction in the number of operating stores. This more than offset large increases in utility expenses, primarily electrical.

Combined direct selling, advertising and general and administrative expenses in both fiscal 1975 and fiscal 1974 were approximately equal in relation to sales. However, direct selling and general and administrative expenses were reduced while advertising charges increased due to the company's more aggressive promotional programs.

The estimated credit related to store closings was $449,000 in fiscal 1975 compared to a charge of $8,560,000 in fiscal 1974. The 1975 credit arose principally from the company's policy of recognizing gains on the disposal of properties in the period realized. The 1974 charge was the result of management's decision to close a number of inefficient stores, the costs of which were charged to income in 1974 under the company's accounting policy adopted at that time as described in Notes 2 and 5 to the Financial Statements.

Other income increased $780,000 primarily due to improved interest income net of expense resulting from the investment of surplus cash in a more favorable market.

In fiscal 1975 the company was able to utilize a portion of its investment tax credit carryforward. Thus, the company's effective tax rate was 30%. In addition, utilization of net operating loss carryforwards resulted in an extraordinary credit of $1,575,000. For financial accounting purposes, further operating loss carryforwards of approximately $11,800,000 are available at this time for future use. No income taxes were provided in fiscal 1974.

Net income in 1975 was $5,708,000 after giving effect to the extraordinary credit arising from the utilization of operating loss carryforwards. Net loss in 1974 was $14,858,000 and includes an extraordinary gain of $572,000 arising from the sale of land, and a charge of $1,964,000, the cumulative effect of the company's change in accounting for closed store expenses.

The assets of the company's pension plan exceed the actuarially computed value of plan liabilities. No charges were required in fiscal 1974 and 1975. The effects of the Employee Retirement Income Security Act of 1975 on future pension costs are not presently determinable.

Fiscal 1974 Compared to Fiscal 1973

In fiscal 1974 sales of $859,598,000 were $10,282,000 greater than in fiscal 1973. The latter was a 53-week period compared to a 52-week period in 1974 and the company promoted heavily after discontinuance of trading stamps in mid-1973. 1974 sales were affected favorably by the rapid increase in inflation and unfavorably both by a net reduction of 37 stores and by severe price competition in the company's market area initiated by a major competitor.

Cost of sales compared to sales volume increased by 1% from fiscal 1973 to fiscal 1974. This was the result of aggressive price competition, rapid inflation and irregularities in the cost and supply of merchandise. The meat area especially experienced reduced sales and gross margin due to high prices and consumer resistance.

In the later months of fiscal 1974 warehousing and transportation costs were seriously affected by the energy crisis and its resultant energy cost increases. Direct selling, advertising and general and administrative expenses were generally stable between the two years. This was so despite increased employee benefits absorbing much of the initial gains of the company's major cost reduction programs which were begun in early 1974.

As discussed in our 1975-1974 comparison, the charge to earnings in 1974 for estimated costs related to store closings was $8,560,000 determined, as described in Notes 2 and 5 to the Financial Statements, under an accounting policy adopted in fiscal 1974. Prior to 1974 costs related to store closings were charged in the period incurred, and no provision for future estimated costs related to closed stores was reflected in income.

Other income net of expense increased in 1974 primarily as a result of the investment of surplus funds arising principally from the results of improved cash management.

The company's net loss in 1974 was $14,858,000 as previously discussed. Net income in 1973 was $35,000 and included an extraordinary loss of $225,000 on the disposal of assets related to the discontinuance of the company's institutional food business.

FIRST NATIONAL STORES INC.

Five Year Summary Of Operations (in thousands)

	Fiscal year ended March 29, 1975	March 30, 1974	March 31, 1973 (53 Weeks)	March 25, 1972	March 27, 1971
Sales	**$ 934,803**	$ 859,598	$ 849,316	$ 842,632	$ 840,744
Costs and expenses:					
Cost of sales, warehousing, transportation and store occupancy expenses	**790,220**	735,148	717,737	712,553	702,788
Direct selling, advertising, general and administrative expenses	**134,121**	123,707	124,509	125,041	124,346
Depreciation and amortization	**6,731**	6,622	6,852	7,494	7,008
Estimated charges (credits) related to store closings	**(449)**	8,560	—	—	—
	930,623	874,037	849,098	845,088	834,142
Operating income (loss)	**4,180**	(14,439)	218	(2,456)	6,602
Other income (expense):					
Interest income	**2,487**	2,107	785	92	235
Interest expense	**(933)**	(1,242)	(856)	(379)	(203)
Other, net	**199**	108	514	(55)	(135)
	1,753	973	443	(342)	(103)
Income (loss) from continuing operations before income taxes	**5,933**	(13,466)	661	(2,798)	6,499
Federal and state income taxes	**1,800**	—	100	(1,345)	2,802
Income (loss) from continuing operations	**4,133**	(13,466)	561	(1,453)	3,697
Loss from discontinued operations, less applicable tax effect	—	—	(301)	(113)	(186)
Income (loss) before extraordinary items and before cumulative effect of change in accounting	**4,133**	(13,466)	260	(1,566)	3,511
Extraordinary items	**1,575**	572	(225)	877	—
Cumulative effect on prior years (to March 31, 1973) of change in method of accounting for costs related to store closings less $1,158 tax effect	—	(1,964)	—	—	—
Net income (loss)	**$ 5,708**	$ (14,858)	$ 35	$ (689)	$ 3,511
Per share of common stock:					
Income (loss) from continuing operations	**$3.32**	$ (9.81)	$ .41	$(1.06)	$2.69
Loss from discontinued operations	—	—	(.22)	(.08)	(.14)
Income (loss) before extraordinary items and cumulative effect of change in accounting	**3.32**	(9.81)	.19	(1.14)	2.55
Extraordinary items	**1.26**	.41	(.16)	.64	—
Cumulative effect of change in method of accounting for store closings	—	(1.43)	—	—	—
Net income (loss)	**$4.58**	$(10.83)	$ .03	$ (.50)	$2.55
Shares outstanding for purposes of computing earnings per share	**1,246,315**	1,372,197	1,372,274	1,372,663	1,375,853
Cash dividends declared per share	**$ .75**	—	—	$ .75	$1.00
Pro forma amounts assuming the change in method of accounting for costs related to store closings had been applied retroactively:					
Income (loss) from continuing operations		$(13,466)	$(227)	$(1,133)	$3,586
Per share of common stock		(9.81)	(.17)	(.83)	2.62
Income (loss) before extraordinary items		(13,466)	(438)	(1,246)	3,400
Per share of common stock		(9.81)	(.32)	(.91)	2.48
Net income (loss)		(12,894)	(618)	(369)	3,400
Per share of common stock		(9.40)	(.45)	(.27)	2.48

Finast

Directors

WILLIAM T. FRENCH, *Chairman of the Board of Directors of the Company*
ALAN L. HABERMAN, *President and Chief Executive Officer of the Company*
LEWIS B. HARDER, *Chairman of the Board and Chief Executive Officer of International Mining Corp. (mining)*
DUNCAN O. McKEE, *Partner in Ballard, Spahr, Andrews & Ingersoll (attorneys)*
EDWARD A. MERKLE, *President of Madison Fund, Inc. (a closed-end investment company)*
WILLIAM B. O'KEEFFE, *Partner in Lyne, Woodworth & Evarts (attorneys)*
JACOB SALIBA, *President of Katy Industries, Inc. (diversified holding company)*
WESLEY A. STANGER, JR., *Registered representative with Edwards & Hanly (investment bankers)*

Officers

WILLIAM T. FRENCH, *Chairman of the Board*
ALAN L. HABERMAN, *President and Chief Executive Officer*
AUSTIN F. LYNE, *Senior Vice President—Services*
KERRY R. LYNE, *Senior Vice President, Secretary and General Counsel*
JOSEPH H. McCARTHY, *Senior Vice President—Supermarkets*
RICHARD L. KENNEY, *Vice President and Treasurer*
RICHARD M. O'KEEFFE, *Vice President*
PETER C. QUINN, *Vice President*
THOMAS F. GRADY, *Controller*

Transfer Agents

THE FIRST NATIONAL BANK OF BOSTON, *100 Federal Street, Boston, Massachusetts 02110*
CHEMICAL BANK, *20 Pine Street, New York, New York 10015*

Registrars

STATE STREET BANK AND TRUST CO., *225 Franklin Street, Boston, Massachusetts 02110*
BANKERS TRUST CO., *280 Park Avenue, New York, New York 10017*

Counsel

LYNE, WOODWORTH & EVARTS, *75 Federal Street, Boston, Massachusetts 02110*
ROPES & GRAY, *225 Franklin Street, Boston, Massachusetts 02110*

Independent Accountants

PRICE WATERHOUSE & CO., *225 Franklin Street, Boston, Massachusetts 02110*

Executive Offices

5 Middlesex Avenue, Somerville, Massachusetts 02143
Tel.: Area Code 617-623-2400

Distribution Centers

Somerville, Massachusetts
South Kearny, New Jersey

Finast®